

INTERNAL REVENUE SERVICE  
District Director

Department of the Treasury

Date:

JUN 21 1999

Employer Identification Number:

Case Number:

Person to Contact/Badge Number:

Contact Telephone Number:

Refer Reply To:

Dear Applicant:

We have considered your application for a [redacted] federal income tax as an organization described under section 501(c)(3) of the Internal Revenue Code.

FACTS:

The information submitted discloses that you were incorporated under [redacted] in order to conduct in discrete corporate form, an activity that had previously been conducted by the [redacted], a [redacted] nonprofit organization exempt under section 501(c)(3) of the Internal Revenue Code.

Article III of your articles of incorporation states that you are organized exclusively for charitable and educational purposes within the meaning of section 501(c)(3) of the Internal Revenue Code, the objects and purposes of which are to be conducted exclusively for the benefit of [redacted], a [redacted] nonprofit corporation, as follows: (a) To promote public awareness and appreciation of the quality and variety of [redacted] through education, research and the collection and dissemination of information; (b) To serve as a forum for the technological and cross-cultural aspects of the art of [redacted]; (c) To encourage responsible use of [redacted] as an [redacted]; and (d) To do and engage in all lawful activities that further or are consistent with the preceding objects and purposes.

Your sole activity is the conduct of a [redacted] called the [redacted]. You stated there are three principal components to the [redacted] (1) public sessions, (2) a professional panel bll, taste testing, and (3) distribution of a substantial program guide. The general public is invited to attend the two-day event. [redacted] from across the country are invited to establish booths from which they dispense one-ounce samples of [redacted]. Each [redacted] answers questions about the technical aspects of [redacted] the historic significance of their [redacted], recipe formulations, and other matters. The festival also includes educational booths that feature [redacted], [redacted], historic information, and current facts. Each [redacted] is permitted to enter [redacted] different categories for evaluation by a panel of professional [redacted]. Awards are given to the [redacted] that represents the best in each category.



The sole member of your organization is the [REDACTED]. The [REDACTED] has the right to elect the members of your board and approve significant corporate matters.

Your income is derived primarily from admissions to the [REDACTED]. Admission entitles each attendee to participate in all activities and free [REDACTED] at each booth. You also receive income from corporate sponsorships which typically range from \$[REDACTED] to \$[REDACTED]. Sponsorship entitles the corporate sponsor to recognition in the program guide, perhaps a banner with the sponsor's name or corporate logo displayed at the festival, several complimentary admissions, and other similar benefits. Other income is received from [REDACTED] fees, merchandise sales and advertising. Your expenses are for event operations, management fee (paid to the [REDACTED]), contract services, printing, publications, postage, shipping, cost of goods sold, and other necessary operational and administrative expenses.

#### ISSUE:

Does the organization qualify for exemption from Federal income tax as an educational organization described under section 501(c)(3), and as a supporting organization under section 509(a)(3) of the Internal Revenue Code? Can the organization qualify for exemption under any other section under section 501(c)?

#### LAW:

Section 501(c)(3) of the Internal Revenue Code describes certain organizations exempt from income tax under section 501(a), and reads in part as follows:

"Corporations, and any community chest, fund, or foundation organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on legislation, (except as otherwise provided in subsection (h), and which does not participate in, or intervene in (including the publishing or distribution of statements), any political campaign on behalf of any candidate for public office."

Section 1.501(c)(3)-1(a)(1) of the income tax Regulations provides that in order to be exempt as an organization described in section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If any organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the Regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(3) of the Regulations provides that the term "educational", as



used in section 501(c)(3), relates to (a) the instruction or training of the individual for the purpose of improving or developing his capabilities, or (b) the instruction of the public on subjects useful to the individual and beneficial to the community.

Section 513 of the Internal Revenue Code defines a trade or business as "...any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under section 501..."

Trade or business has the same meaning for the purpose of determining whether a particular expense is a deductible trade or business expense under Internal Revenue code section 162 and includes any activity carried on for the production of income from the sale of goods or in the performance of services. An activity doesn't lose identity as a trade or business merely because it's carried on within a larger aggregate of similar activities or within a larger complex of other endeavors which may or may not be related to the exempt purpose. See Income Tax Regulations 1.513-1(b).

In construing the meaning of the phrase "exclusively for educational purposes" in *Better Business Bureau v. U.S.*, 326 U.S. 279 (1945), Ct. D. 1650, C.B. 1945, 375, the Supreme Court of the United States said, "This plainly means that the presence of a single non-educational purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly educational purposes." This rationale applies equally to any category of charitable purpose under section 501(c)(3).

#### ANALYSIS:

Your sole activity is preparing and conducting an annual [REDACTED] (the [REDACTED]), open to the general public. A copy of the festival program you provided with your application showed the floor plan and the various activities and events which takes place during the festival. Based on a review of the floor plan, the "educational" aspects of the festival were located in a separate section of the exhibition hall. This section included the demonstration area, information displays, [REDACTED] displays, [REDACTED] libraries, and book signings. Although the main floor of the exhibition hall does have some video booths and a presentation area, the majority of the floor space was devoted almost entirely of exhibitor booths of the various [REDACTED] and [REDACTED], and food and merchandise booths. The overall format and presentation of the event is no different than a convention and trade show carried on in a commercial manner.

A letter dated [REDACTED] from your attorney, [REDACTED] he stated that substantially all of your activities are educational in nature. The principal purpose of the [REDACTED] is to promote public awareness and appreciation for the quality and diversity of [REDACTED] through education, research, and collection and dissemination of information, to serve as a forum for the technological and cross-cultural aspects of the art of [REDACTED] and to encourage the responsible use of [REDACTED] as an [REDACTED]. He further stated that one of the aspects of the Festival that distinguishes it from a convention or trade show is that most of the [REDACTED] that are displayed at the [REDACTED] are generally not available to the general public except in extremely small geographic markets. He goes on to say that of the hundreds of [REDACTED] that occupy booths at the [REDACTED], probably [REDACTED] percent or more are small [REDACTED] or [REDACTED] whose [REDACTED] are sold only in one restaurant, [REDACTED], or similar location in their home cities, and most do not produce [REDACTED] in sufficient quantities for sale or



[REDACTED]

distribution beyond their particular outlet.

CONCLUSION:

Although there are some educational activities and events that take place during the Festival, it is not exclusively educational as described under section 501(c)(3) of the Internal Revenue Code. The fact that many of the [REDACTED] are uniquely [REDACTED] and not available for sale or distribution beyond their particular outlet does not deter the fact that it is the [REDACTED] themselves who benefit from exposure at the event. The [REDACTED] serves as an outlet to promote their individual product.

Accordingly, based on the information submitted, it is held that you do not meet the requirements for exemption as an organization described under section 501(c)(3) of the Internal Revenue Code because you are not operated exclusively for educational purposes. Whether you qualify as a supporting organization under section 509(a)(3) of the Code is irrelevant, since we have determined you do not qualify for exemption under section 501(c)(3).

We have also considered whether you would qualify for exemption under any other section under 501(c) and have determined that you would not meet the qualifications under any other section. However, you may want to reconsider making the [REDACTED] a part of the activity of the [REDACTED], as it originally had been.

If you are in agreement with this proposed determination, we request that you sign and return the enclosed agreement, Form 6018 (Consent to Proposed Adverse Action). Please note the instructions for signing on the reverse side of the form.

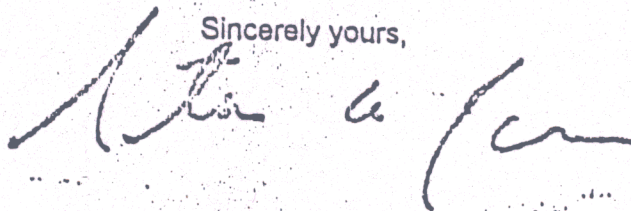
If you do not agree with this proposed determination, we recommend that you request a hearing with our office of Regional Director of Appeals. Your request for a hearing should include a written appeal giving the facts, law, and any other information to support your position, as explained in the enclosed Publication 892. You will then be contacted to arrange a date for a hearing. The hearing may be held at the office of Regional Director of Appeals or, if you request, at a mutually convenient District office. A self-addressed envelope is enclosed.

If you do not appeal this proposed determination within 30 days from the date of this letter, as explained in Publication 892, this letter will become our final determination on this matter. Further, if you do not appeal this determination within the time period, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the district court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service".

[REDACTED]

If you have any questions, please contact the person whose name and telephone number are shown on the heading of this letter.

Sincerely yours,



Steven A. Jensen  
District Director

Enclosure:  
Publication 892  
Form 6018  
Envelope

cc: [REDACTED]